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No. 105

IN THE

SUPREME COURT OF THE UNITED STATES.

EDWARD C. HEARD and
CORA L. HEARD,
Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION FOR WRIT OF CERTIORARI

To the United States Court of Appeals
for the Eighth Circuit.

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To the United States Court of Appeals for the Eighth Circuit.

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

Your petitioners, Edward C. Heard and Cora L. Heard, respectfully pray that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Eighth Circuit in the cause styled "Edward C. Heard and Cora L. Heard, Petitioners v. Commissioner of Internal Revenue, Respondent," affirming the judgment of the Tax Court of the United States.

The opinion of the Court of Appeals is reported at 326 F. 2d 962, and a copy thereof is appended.

JURISDICTION

The judgment of the Court of Appeals is dated January 31, 1964, and was entered on the same date. Jurisdiction of this Court to review the judgment of the Court of Appeals is conferred by the Act of June 25, 1948, c. 646, 62 Stat. 928, 28 U. S. C. Sec. 1254.

QUESTION PRESENTED

The question presented for review is whether monthly payments received by the petitioner Edward C. Heard during the year 1958 under the Civil Service Retirement Act, as amended, constitute annuity income taxable under Section 72 (d) of the Internal Revenue Code of 1954, or are otherwise includible in petitioner's gross income.

STATUTES INVOLVED

The statutes involved are Sections 61 (a) and 72 (a) and (d) of the Internal Revenue of 1954, 26 U. S. C. 61 (a), 72 (a), (d); and the Civil Service Retirement Act, as amended, c. 349, 46 Stat. 468, 5 U. S. C., 1952 ed., Sec. 691 et seq.

The pertinent text of the above statutes is appended.

STATEMENT OF THE CASE

Petitioners, Edward C. and Cora L. Heard, are husband and wife. They reside in St. Louis, Missouri, and filed a joint Federal income tax return for the year 1958 with the District Director of Internal Revenue in that city. For convenience, Edward C. Heard will hereinafter be referred to as petitioner.

Petitioner was a member of the armed forces engaged in the military service of the United States from October 2, 1917, until about October 2, 1919. He was an employee in the classified civil service of the United States from on or about September 15, 1929, until on or about August 15, 1952. Thus, he had been in the service of the United States (including military service prior to 1920 and classified civil service) for 24 years, 10 months, and 6 days prior to August 15, 1952, when he retired from such service.

Retirement deductions withheld from petitioner's salary pursuant to the Civil Service Retirement Act (the "Retirement Act") during all of his civilian Federal service totaled $3,639. No such deductions were withheld from his pay while he was in military service.

By virtue of his service, petitioner was entitled to retirement benefits under the Retirement Act and, as permitted by that Act, upon retirement on August 15, 1952, he elected to receive payments commencing May 1, 1956, immediately after he attained age 62, in the amount of $181 per month as long as he might live. This amount was increased by law commencing August 1, 1958, to $199 per month.

From May, 1956, when petitioner's payments commenced, through December 31, 1957, petitioner received civil service retirement benefits totaling $3,620, that is, an amount only $19 less than the total of retirement deductions withheld from his salary.

During the calendar year 1958, petitioner received monthly payments under the Retirement Act totaling $2,244. He did not include any part of this amount in income on his Federal income tax return for that year.

On February 9, 1961, the respondent issued a statutory notice of deficiency in petitioner's Federal income tax

for the year 1958 in the amount of $509.07, asserting that $2,225 of the total amount of $2,244 received by petitioner was includible in petitioner's gross income under Section 72 (d) of the Internal Revenue Code, applicable to "annuities".

Petitioner, acting *pro se*, petitioned the Tax Court of the United States for a redetermination of the asserted deficiency. The Tax Court, in an opinion filed April 10, 1963, sustained the respondent's determination, holding that amounts received by petitioner in excess of amounts withheld from his salary during his civil service are includible in his gross income pursuant to Section 72(d) of the Internal Revenue Code of 1954.

Petitioner petitioned the Court of Appeals to review the decision of the Tax Court. The Court of Appeals affirmed the decision of the Tax Court, but on the ground that civil service retirement benefits are taxable as gross income under Section 61(a) of the Code. The Court of Appeals declined to rule on the applicability of Section 72(d), relied on by the respondent and the Tax Court, to civil service retirement benefits.

REASON FOR ALLOWANCE OF THE WRIT.

The reason relied on for allowance of the writ of certiorari is, and petitioners allege and state, that the Court of Appeals in this case has decided an important question of federal law which has not been, but should be, settled by this Court.

ARGUMENT.

The question of federal law involved in the instant case is, "Are civil service retirement benefits subject to tax?"

The importance of this question appears readily from its mere statement. It is unnecessary to belabor the well-known facts, that a large and respected class of the population of the nation is receiving or expects to receive such benefits in large, total amounts. The question has not been determined authoritatively. The statutory expressions of Congressional intent are new in the Internal Revenue Code of 1954. They confirm in part and repudiate in part previous principles, and codify the whole, making previous, fragmentary expressions of administrative policy, even practice, if any existed, illusory and weightless.

Further, the considerations properly leading to the answer to the question are of importance: the nature of differences required by due process of law to justify a discrimination in income tax; the nature of income and civil service retirement payments; the construction of a codification of law, as compared to a general statute.

The includibility of civil service retirement benefits in the measure of income tax is questioned here on two grounds: first, is there, in the case of such benefits, income within the meaning of the Internal Revenue Code and the Sixteenth Amendment to the Constitution? Second, even if there is income, is discrimination between civil service retirement benefits and social security retirement benefits, which are similar to the point of identity in their material aspects, intended by Congress, or, if intended, permissible under the Fifth Amendment to the Constitution?

It is submitted that the Court ought to consider the question. The considerations leading to the answer (prop-

erly, it is believed, in the negative) ought to be presented fully to the Court. Here, they need be outlined only sufficiently to demonstrate the existence of a serious question.

First: Is there income within the meaning of the Sixteenth Amendment to the Constitution and the Internal Revenue Code?

From the beginnings of United States income taxation a century ago, the dichotomous significance of "income" as a subject of tax have been known: whether it was, on the one hand, receipts (including gifts, inheritances, and the like), or, on the other hand, "annual wealth," as gain from a source. This dichotomy culminated in the conflict of the majority with the minority of this Court in **Pollock v. Farmers Loan & Trust Co.**, 157 U. S. 429, 158 U. S. 601, in which the majority held the income tax a direct tax because it viewed the source of income as the subject of tax, so that the tax was on capital or on labor; but the minority viewed the payment or receipt as the subject of tax, so that the tax was on circulation of money. Compare **Gray v. Darlington**, 82 U. S. (15 Wall.) 63, and **Veazie Bank v. Fenno**, 75 U. S. (8 Wall.) 533.

The view of the majority of the Court in **Pollock v. Farmers Loan & Trust Co.**, *supra*, was embodied in the Sixteenth Amendment to the Constitution, authorizing Congress to lay and collect taxes "on incomes from whatever source derived," thus excluding the notion of income from no source whatever, as a mere payment, a gift or inheritance. The generally recognized source of income (annual wealth) is "the application of labor to a capital stock," or "capital or labor or both combined," and no one has yet imagined a source of income not within the broad, developed understanding of these words. It is now unnecessary to speculate whether such a source could exist, since it has been found easier to extend the meaning

of the words "capital and labor" to include any possible source, so that such things as associations of numerous people which enable an insurance company to operate profitably, or a list of trappers which enables a fur company to trade, or going business, may, since they are of value, be considered capital.

It should now be affirmed that a mere payment, or its correlative receipt, is not income. The tax laws are far developed on the basis that income is **gain**, the yield of a source. The gain is consideration rendered—services, applied directly or indirectly to a capital stock—and the payment given and received, if it is for services, measures the value of the services by the agreement of the parties, and, within limits, fixes the time for taxation of the services as income. The very color of the words—wages, compensation, remuneration—evokes a picture of balance —*quid pro quo*.

Hence, to determine whether or not civil service benefits are includible in the measure of income tax (without regard to the question **when** they are so includible), the inquiry is made whether or not it is in consideration, or the *quid pro quo*, or wages, of services. Is it on one side of the scale the balance of services on the other?

In the instant case, part of the included services were rendered prior to the enactment of the Civil Service Retirement Act; that Act was amended from time to time while the petitioner was in service and thereafter. The purpose of the provisions was admittedly not to compensate civil servants for their current or past work, but to provide for a worthy class of the public in retirement and to make room for advancement of younger civil servants. It will therefore be urged that the civil service retirement benefits are not wages, compensation, or *quid pro quo* of labor or work, and hence not the occasion for computation of the labor or work as gain or income. There is no

weight on the other side of the scale, to balance this payment, made for the public welfare; no consideration or *quid pro quo* furnished by or for petitioner.

Second: Does taxation of civil service retirement benefits constitute unlawful discrimination?

It will be shown that the civil service retirement benefits are **in lieu of** social security retirement benefits, which are not includible in the measure of taxable income. Even if the civil service benefits may as receipts be considered income, they are in this and in every other material respect no different from social security benefits, which are not subject to tax. A discrimination between two classes of citizens on the basis of their prior, past employment or condition of servitude, and not on the basis of any present difference, ought not be imputed to Congress, and under the language of the Internal Revenue Code is not required. Equality is the equity, justice, and due process of law in taxation, and a discrimination in tax, unless based on a material difference, ought not be sustained.

Many years ago tax assessors in various states conceived that, if they consistently valued property for taxation at a fraction of its value, then one taxpayer could not complain if his property was valued at a larger fraction of its value as long as it was valued at less than full value. It was suggested that his only remedy was to procure an increase in the valuation of others' property. The Courts, of course, were not so easily circumvented, and readily subordinated even constitutional provisions that property be assessed at full value to the requirements of equality and uniformity.

Similarly here: social security benefits are systematically excluded from the measure of their recipients' taxable incomes. Therefore, petitioner's similar or identical

benefit must be excluded from the measure of his taxable income, and it is no practical answer that the social security benefits are or ought to be includible in the measure of their recipients' income tax. Equality and due process can be enforced only by striking down the unfair, relative burden imposed by the systematic discrimination.

RELIEF PRAYED

Wherefore, your petitioners respectfully pray that a writ of certiorari be issued out of and under the seal of this Honorable Court, directed to the United States Court of Appeals for the Eighth Circuit, to review its decision in the case numbered and entitled on its docket No. 17,404, Edward C. Heard and Cora E. Heard, Petitioners, v. Commissioner of Internal Revenue, Respondent; and that the judgment of said Court in said case be reversed by this Honorable Court, and that your petitioners may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

Respectfully submitted,

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.....

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APPENDIX.

I. Opinion of the Court of Appeals:

United States Court of Appeals
For the Eighth Circuit.

No. 17,404

Edward C. Heard and Cora L. Heard, Petitioners, v. Commissioner of Internal Revenue, Respondent.	On Petition for Review of the Decision of the Tax Court of the United States.

[January 31, 1964.]

Before Van Oosterhout, Matthes and Mehaffy, Circuit Judges.

Matthes, Circuit Judge.

The broad question presented in this review proceeding is whether the amount received by Edward C. Heard (hereinafter referred to as "taxpayer") under the Civil Service Retirement Act (Act) in excess of the amount contributed by him to the retirement fund is taxable income. The Commissioner ruled it was taxable and assessed a deficiency. The Tax Court upheld the deficiency assess-

ment, 40 T. C. 7 (1963), and for reasons hereinafter stated, we affirm the Tax Court's decision.

Taxpayer Edward C. Heard and Cora L. Heard, husband and wife, filed a joint federal income tax return for the year 1958.

Taxpayer served in the armed forces of the United States from October 2, 1917, until about October 2, 1919. From on or about September 15, 1929, until on or about August 15, 1952, he was an employee in the classified civil service of the United States Government. Including military service prior to 1920 and classified civil service, his total service with the United States prior to his retirement on August 15, 1952, was 24 years, 10 months and 6 days.

Taxpayer, who reached the age of 62 on April 23, 1956, and who was entitled to benefits under the Act, elected—on or about August 15, 1952—to receive an annuity commencing on May 1, 1956. The annuity amounted to $181 per month, which was increased by law, commencing August 1, 1958, to $199 per month. During the year 1958, taxpayer received payments under the Act totaling $2,244. During 1956 and 1957, the payments he received totaled $3,620.

Retirement deductions withheld from taxpayer's salary during his civilian service with the Federal Government totaled $3,639.01. No such deductions were withheld from his pay while he was in the military service.

Relevant to the issue before us are §§ 72 and 61 (a) of the Internal Revenue Code of 1954.

The pertinent part of § 72 reads as follows:

"(a) **General rule for annuities**—

"Except as otherwise provided in this chapter, gross income includes any amount received as an an-

nuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract.

"(d) **Employees' annuities.**—

"(1) Employee's contributions recoverable in 3 years.—Where—

"(A) part of the consideration for an annuity, endowment, or life insurance contract is contributed by the employer, and

"(B) during the 3-year period beginning on the date (whether or not before January 1, 1954) on which an amount is first received under the contract as an annuity, the aggregate amount receivable by the employee under the terms of the contract is equal to or greater than the consideration for the contract contributed by the employee,

then all amounts received as an annuity under the contract shall be excluded from gross income until there has been so excluded (under this paragraph and prior income tax laws) an amount equal to the consideration for the contract contributed by the employee. Thereafter all amounts so received under the contract shall be included in gross income."

Section 61 reads in pertinent part as follows:

"(a) **General definition.**—

"Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

"(9) Annuities;"

Acting under § 72(d), supra, the Commissioner determined that the amounts received by taxpayer pursuant to

the Act were annuities within the meaning of that Code provision, that $2,224.80 of the $2,244 received in 1958 was includable as gross income, and he accordingly assessed the deficiency.

After discussion and consideration of taxpayer's contentions, the Tax Court concluded that:

> "The petitioner's annuity is within the provisions of section 72(d). During the three-year period beginning with the first payment the aggregate amount receivable by him was greater than the amount of his contributions to the retirement fund through withholding from his salary. These amounts were correctly excluded from his gross income until his contributions were recovered. Thereafter all the amounts he received should be included in gross income."

However, the Tax Court also dealt with the applicability of present § 61 of the 1954 Code, supra, in this language:

> "The petitioner contends that the Congress did not intend to tax civil service retirement annuities. There is no indication in the original Retirement Act, which was enacted in 1920, that such was the intent. The Revenue Act of 1918, 40 Stat. 1057, then in effect, defined gross income as 'gain or profits and income derived from any source whatever.' Sec. 213(a). The courts have construed the taxing acts as applying to all gains except those specifically exempted."

Basically, taxpayer contends that § 72 of the 1954 Internal Revenue Code applies only to annuities under "an

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[1] As we have seen, taxpayer received benefits under the Act in 1956, 1957 and 1958 totaling $5,884 and made contributions to the fund totaling $3,659.40. The Commissioner based the deficiency assessment upon the amount received by taxpayer in 1958 in excess of the total amount contributed by him to the civil service fund.

annuity, endowment, or life insurance **contract**;" that the amount in question received by taxpayer under the Act is a gratuitous pension and not an annuity paid pursuant to a **contractual** obligation within the meaning of § 72; that "section 72 does fully cover the annuities taxable as income, and unless an annuity or pension is within the provisions of that section, it ought not to be deemed income at all;" that Social Security benefits are exempt from income tax, and no difference between such benefits and the benefits here involved justifies a discriminatory treatment between the two retirement programs; and that neither Social Security nor civil service benefits measure or can be considered to be "income taxable under **section 61** of the Internal Revenue Code or the Sixteenth Amendment to the Constitution."

In our view, taxpayer's contention that the amount received by taxpayer over and above his contributions represents a non-taxable gift from the Government is wholly untenable.[4]

The Supreme Court has announced that a non-taxable gift within the meaning of the Code "proceeds from detached and disinterested generosity, 'from affection, respect, admiration, charity or similar impulses.' **Commissioner v. Duberstein**, 363 U. S. 278, 285 (1960). Taxpayer, however, argues that the amounts here in controversy—even if paid pursuant to both legal and moral obligation—are "nevertheless 'gifts' in the sense that they are not income."

The language of the Act (see 5 U. S. C. A., §§ 691 et seq., now 5 U. S. C. A., §§ 2251-2268) in its entirety completely refutes the assertion that retirement benefits paid thereunder proceed from dominantly a gratuitous intent, or

[4] Under § 102 of the Internal Revenue Code of 1954, "Gross income does not include the value of property acquired by gift

can—for income tax purposes—be in any sense considered as gifts. The Act specifically denominates the benefits as "an annuity;" participation in the retirement program is compulsory for most civilian Government employees; the retirement fund—from which the annuities are paid—consists basically of automatic deductions from the salaries of all participating employees and of regular appropriations by the Government; the point of time when an employee becomes entitled to his annuity depends upon his age, or date of disability, and upon his length of service; and the amount to which the employee is entitled is primarily based upon his salary and duration of service.

Additionally, the legislative history of the Act indicates that Congress was in large measure concerned with obtaining benefits for the Government through the creation of a more efficient civil service. Among such desired benefits was the hope of placing federal employment on a comparable, competitive level with private employment. Civil service benefits are "... obviously, not mere gratuities. . . . Rather, the Government in its role of employer has, like many other employers today, set up a retirement plan under which both the employees and the employer contribute." **United States v. Price**, 4 Cir., 288 F. 2d 448, 450-451 (1961), affirming, E. D. Va., 179 F. Supp. 309 (1959). See also, **Dismuke v. United States**, 297 U. S. 167, 170 (1936).

Gross income is defined very broadly by § 22(a) of the 1939 Code and by § 61(a) of the 1954 Code, and includes all income from whatever source derived. **Haberman Farms, Inc. v. United States**, 8 Cir., 305 F. 2d 787, 790 (1962); **Schoenberg v. C. I. R.**, 8 Cir., 302 F. 2d 416, 418 (1962). Courts have repeatedly held that through this sweeping language, Congress intended to "tax all gains except those specifically exempted." **Commissioner v. Glenshaw Glass Co.**, 348 U. S. 426, 429-430 (1955); **United**

Grocers, Ltd. v. United States, 9 Cir., 308 F. 2d 634, 637 (1962); **Simpson v. United States**, 7 Cir., 261 F. 2d 497, 500 (1958), cert. denied 359 U. S. 944 (1959). And the exemptions provided for should be construed with restraint in accordance with the Congressional purpose to tax income comprehensively. **Commissioner v. Jacobson**, 336 U. S. 28, 49 (1949); **Omaha Public Power District v. O'Malley**, 8 Cir., 232 F. 2d 805, 809 (1956), cert. denied 352 U. S. 837 (1956); **Simpson v. United States**, supra, 261 F. 2d at 500.

The only exemption that could possibly have application here is the gift exemption—taxpayer cites no other specific provision, and as previously shown, in our view the controverted annuity received by taxpayer pursuant to the Act cannot in any sense be considered as a gift. See and compare, **Commissioner v. LoBue**, 351 U. S. 243, 246 (1956).

Moreover, since shortly after enactment of the civil service retirement program—similar to the present system, various administrative rulings, decisions, and regulations have consistently held that civil service retirement annuites are taxable under the general provision defining gross income (presently, § 61), and—more recently, have held that such annuities are taxable within the contemplation of § 72 of the 1954 Code.[3]

Examination of the history of the Code provisions dealing with annuities reveals that they have periodically been reenacted with various modifications since the Commissioner first ruled that civil service benefits were taxable;

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[3] See and compare, T. D. 3112, 4 Cum. Bull. 76 (1921); I. T. 2084, XV-1 Cum. Bull. 87 (1936); T. D. 5208, 1943 Cum. Bull. 65; Treas. Reg. 111 (1939 Code), § 29.22 (b) (2)-2; Treas. Reg. 118 (1939 Code), § 39.22 (b) (2)-2 (x) (1); Treas. Reg. on Income Tax (1954 Code), § 1.61-11; Treas. Reg. on Income Tax (1954 Code), § 1.72-2 (a) (3) (iii) and (iv).

that complete or partial exemption of such benefits has been urged upon Congress; and that despite knowledge of the Commissioner's rulings and regulations and despite efforts by exemption proponents, Congress has failed to grant such an exemption as is here contended for by taxpayer. If Congress had been dissatisfied with the rulings and regulations—administrative interpretations which under the circumstances here should be accorded considerable weight, it had sufficient time and opportunity to take action. **Commissioner v. South Texas Co.**, 333 U. S. 496, 501 (1948); **Iverson's Estate v. Commissioner**, 8 Cir., 255 F. 2d 1, 3 (1958), cert. denied 358 U. S. 893 (1958); **United States v. Stowe-Woodward, Inc.**, 1 Cir., 306 F. 2d 678, 680-681 (1962), cert. denied 371 U. S. 949 (1963). "This bespeaks congressional approval" of the Commissioner's tax treatment of the annuities. **Corn Products Co. v. Commissioner**, 350 U. S. 46, 53 (1955); **F. Strauss & Son, Inc., of Ark. v. Commissioner**, 8 Cir., 251 F. 2d 724 (1958), affirmed sub nom., **Cammarano v. United States**, 358 U. S. 498 (1959); **Miller v. Commissioner**, 4 Cir., 144 F. 2d 287, 289-290 (1944).

Although—as previously noted—Congress did not give complete tax exemption to civil service annuities, in enacting § 37 of the 1954 Code, 26 U. S. C. A., § 37, it did allow a certain "credit" for such benefits. Section 37 was enacted partially in response to urging by various proponents of complete exemption for civil service annuities. Testimony before Congressional committees by such proponents clearly indicates that civil service benefits were not then exempt. In 1953, before a House Hearing on General Revenue Revision, the President of the Retirement Federation of Civil Service Employees of the United States Government, stated in part:

> "We want to go on record as endorsing the general principle of **removing** taxes from annuities of em-

> ployees who are living on annuities, to extend the same benefits that are given under the social security and railroad retirement." (Emphasis supplied.)[4]

And it is equally certain that Congress—in enacting § 37—intended a **partial** adjustment, but not the complete exemption here asserted by taxpayer. In reporting their recommendations, the committees to which the bill that became § 37 was referred in both the House and the Senate, stated, in effect:

> "Under existing law benefits payable under the social-security program and certain other retirement programs of the Federal Government are exempt from income tax. Your committee believes that the tax-exempt status of such benefits discriminates against persons receiving retirement pensions under other publicly administered programs. . . . Your committee has sought to adjust this differential tax treatment by extending a **limited** exemption, by means of a tax credit, to all forms of retirement income." (Emphasis supplied).[5]

But taxpayer argues that § 37 does not "eliminate discrimination between recipients of social security benefits and recipients of civil service benefits if the latter are taxable income," and that such discrimination is repugnant to the Fifth Amendment to the Constitution. This contention is without merit for the tax treatment distinction

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[4] 3 House Hearings on General Revenue Revision (1953), pp. 1979-1980 (see also pp. 1959-1963, 1966-1974, 1971-1973). Additionally, see 1 Senate Hearings on the Internal Revenue Code of 1954, pp. 241, 630; 2 Senate Hearings on the Internal Revenue Code of 1954, pp. 774-777, 779, 780; 4 Senate Hearings on the Internal Revenue Code of 1954, pp. 2139-2141, 2272-2273, 2274.

[5] H. Rep. No. 1337, 83 Cong., 2d Sess., pp. 7-8, A16-A17 (3 U. S. C. Cong. & Adm. News (1954) 4017, 4032, 4152-4153); S. Rep. No. 1622, 83 Cong., 2d Sess., pp. 8-9, 165-166 (3 U. S. C. Cong. & Adm. News (1954) 4621, 4637, 4796-4801).

complained of here is not arbitrary or capricious. See and compare, **Barclay & Company v. Edwards**, 267 U. S. 442, 450 (1924); **Foley Securities Corp. v. Commissioner**, 8 Cir., 106 F. 2d 731, 735-736 (1939).

Furthermore, the Tax Court has held that similar payments under other retirement programs are taxable income to the recipients. **Brittelle v. Commissioner**, 32 T. C. 1332 (1959) (public school teacher's annuity as provided for by Wisconsin statute); **Curtis v. Commissioner**, 8 T. C. 266 (1947) (widow's pension from policemen and firemen's relief fund, Washington, D. C.). Compare also, **Goethals v. United States**, Ct. Cl., 147 F. Supp. 757 (1957) (army officer's retirement pay).

Additionally, the Government claims, and the Tax Court found, that § 72 of the 1954 Code applies to the civil service annuity here in controversy. Taxpayer—as noted—contends that § 72 applies only to annuity **contracts** and that civil service retirement annuities are not paid pursuant to contract, citing **Dismuke v. United States**, supra, 297 U. S. 167. Since we have demonstrated and determined that the annuity is taxable under § 61 (a), the applicability of § 72 under the facts of this case need not be explored nor decided. For whether or not § 72 applies, the result is the same—i. e., the amount received under the Act in excess of the amount contributed to the retirement program by taxpayer is taxable income.

Affirmed.

A true copy.

Attest:

Clerk, U. S. Court of Appeals, Eighth Circuit.

2. Text of statutes involved:

Sec. 61. Gross Income Defined.

(a) **General Definition.**—Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

(1) Compensation for services, including fees, commissions, and similar items;

* * * * * * * *

(9) Annuities;

* * * * * * * *

(26 U. S. C., 1958 ed., Sec. 61.)

Sec. 72. Annuities; Certain Proceeds of Endowment and Life Insurance Contracts.

(a) **General Rule for Annuities.**—Except as otherwise provided in this chapter, gross income includes any amount received as an annuity (whether for a period certain or during one or more lives) under an annuity, endowment, or life insurance contract.

* * * * * * * *

(d) **Employees' Annuities.**—

(1) Employee's contributions recoverable in 3 years.—

Where—

(A) part of the consideration for an annuity, endowment, or life insurance contract is contributed by the employer, and

(B) during the 3-year period beginning on the date (whether or not before January 1, 1954) on which an amount is first received under the contract as an annuity, the aggregate amount receivable by the employee under the terms of

the contract is equal to or greater than the consideration for the contract contributed by the employee,

then all amounts received as an annuity under the contract shall be excluded from gross income until there has been so excluded (under this paragraph and prior income tax laws) an amount equal to the consideration for the contract contributed by the employee. Thereafter all amounts so received under the contract shall be included in gross income.

* * * * * * *

(26 U. S. C., 1958 ed., Sec. 72.)

Civil Service Retirement Act, c. 349, 46 Stat. 468:

Sec. 1 [as amended by Sec. 1, Act of February 28, 1948, c. 84, 62 Stat. 48]. (a) Any officer or employee to whom this Act applies who shall have attained or shall hereafter attain the age of sixty years and have rendered at least thirty years of service computed as prescribed in section 5 of this Act, or who shall have attained or shall hereafter attain the age of sixty-two years and have rendered at least fifteen years of such service, shall, upon separation from the service, be paid an annuity computed as provided in section 4 of this Act.

* * * * * * *

(5 U. S. C., 1952 ed., Sec. 691.)

Sec. 3 [as amended by Sec. 3, Act of January 24, 1942, c. 16, 66 Stat. 13]. (a) This Act shall apply to all officers and employees in or under the executive, judicial, and legislative branches of the United States Government. * * * * * *

* * * * * * * *

(5 U. S. C., 1952 ed., Sec. 693.)

Sec. 4 [as amended by Sec. 4, Act of February 28, 1948, supra]. (a) The annuity of an officer or employee

retired under this Act shall be a life annuity, terminable upon the death of the annuitant and shall be an amount equal to the following: (1) 1½ per centum of the average annual basic salary, pay, or compensation received by the officer or employee during any five consecutive years of allowable service at the option of the officer or employee multiplied by the years of service, or (2) 1 per centum of the average annual basic salary, pay, or compensation received by the officer or employee during any five consecutive years of allowable service at the option of the officer or employee multiplied by the years of service, plus a sum equal to $25 for each year of such service: **Provided**, That in no case shall the annuity exceed an amount equal to 80 per centum of the highest average annual basic salary, pay, or compensation received by the officer or employee during five consecutive years of allowable service.

* * * * * * * *

(5 U. S. C., 1952 ed., Sec. 733.)

Sec. 7 [as amended by Sec. 7, Act of February 28, 1948, supra].

* * * * * * * *

(b) Should any officer or employee to whom this Act applies after having rendered at least twenty years of creditable civilian service and before becoming eligible for retirement under section 1 (a) of this Act become separated from the service, such officer or employee shall be paid a deferred annuity beginning at the age of sixty-two years, or the age at separation if beyond the age of sixty-two, computed as provided in section 4 (a).

* * * * * * * *

(5 U. S. C., 1952 ed., Sec. 733.)

Sec. 10 [as amended by Sec. 10, Act of February 28, 1948, supra]. Beginning as of July 1, 1942, there shall

be deducted and withheld from the basic salary, pay, or compensation of each officer or employee to whom this Act applies a sum equal to 5 per centum of such officer's or employee's basic salary, pay, or compensation: **Provided**, That from and after the first day of the first pay period which begins after June 30, 1948, there shall be deducted and withheld from the basic salary, pay, or compensation of each officer or employee to whom this Act applies a sum equal to 6 per centum of such officer's or employee's basic salary, pay, or compensation. The amounts so deducted and withheld * * * shall * * * be deposited in the Treasury of the United States to the credit of the civil-service retirement and disability fund created by the Act of May 22, 1920, and said fund is hereby appropriated for the payment of annuities, refunds, and allowances as provided in this Act.

* * * * * * *

Every employee coming within the provisions of this Act shall be deemed to consent and agree to the deductions from salary, pay, or compensation as provided herein, and payment less such deductions shall be a full and complete discharge and acquittance of all claims and demands whatsoever for all regular services rendered by such employee during the period covered by such payment, except the right to the benefits to which he shall be entitled under the provisions of this Act. * * *

(5 U. S. C., 1952 ed., Secs. 719 and 722.)

Sec. 11. The Secretary of the Treasury shall invest from time to time, in interest-bearing securities of the United States or Federal farm loan bonds, such portions of the "civil-service retirement and disability fund" as in his judgment may not be immediately required for the payment of annuities, refunds, and allowances as herein provided, and the income derived from such investments shall constitute a part of said fund for the

purpose of paying annuities and of carrying out the provisions of section 12 of this Act.

(5 U. S. C., 1952 ed., Sec. 720.)

Sec. 16 [as affected by Ex. Ord. No. 6670, April 7, 1934, issued under the authority of Secs. 401-409, Act of March 3, 1933, c. 212, 47 Stat. 1489]. The Civil Service Commission is hereby authorized and directed to select three actuaries, one of whom shall be the Government actuary, to be known as the Board of Actuaries, whose duty it shall be to annually report upon the actual operations of this Act, with authority to recommend to the Civil Service Commission such changes as in their judgment may be deemed necessary to protect the public interest and maintain the system upon a sound financial basis, and they shall make a valuation of the "civil-service retirement and disability fund" at intervals of five years, or oftener if deemed necessary by the Civil Service Commission; they shall also prepare such tables as may be required by the Civil Service Commission for the purpose of computing annuities under this Act. The compensation of the members of the Board of Actuaries, exclusive of the Government actuary, shall be fixed by the Civil Service Commission.

(5 U. S. C., 1952 ed., Sec. 731.)

Sec. 17 [as affected by Ex. Ord. No. 6670, April 7, 1934, issued under the authority of Secs. 401-409, the Act of March 3, 1933, supra, and as amended by Sec. 301 (90), Budget and Accounting Procedures Act of 1950, c. 946, 64 Stat. 832]. * * *

* * * * * * *

The Civil Service Commission shall submit estimates of the appropriations necessary to finance the retirement and disability fund and to continue this Act in full force and effect.

(5 U. S. C., 1952 ed., Sec. 730.)

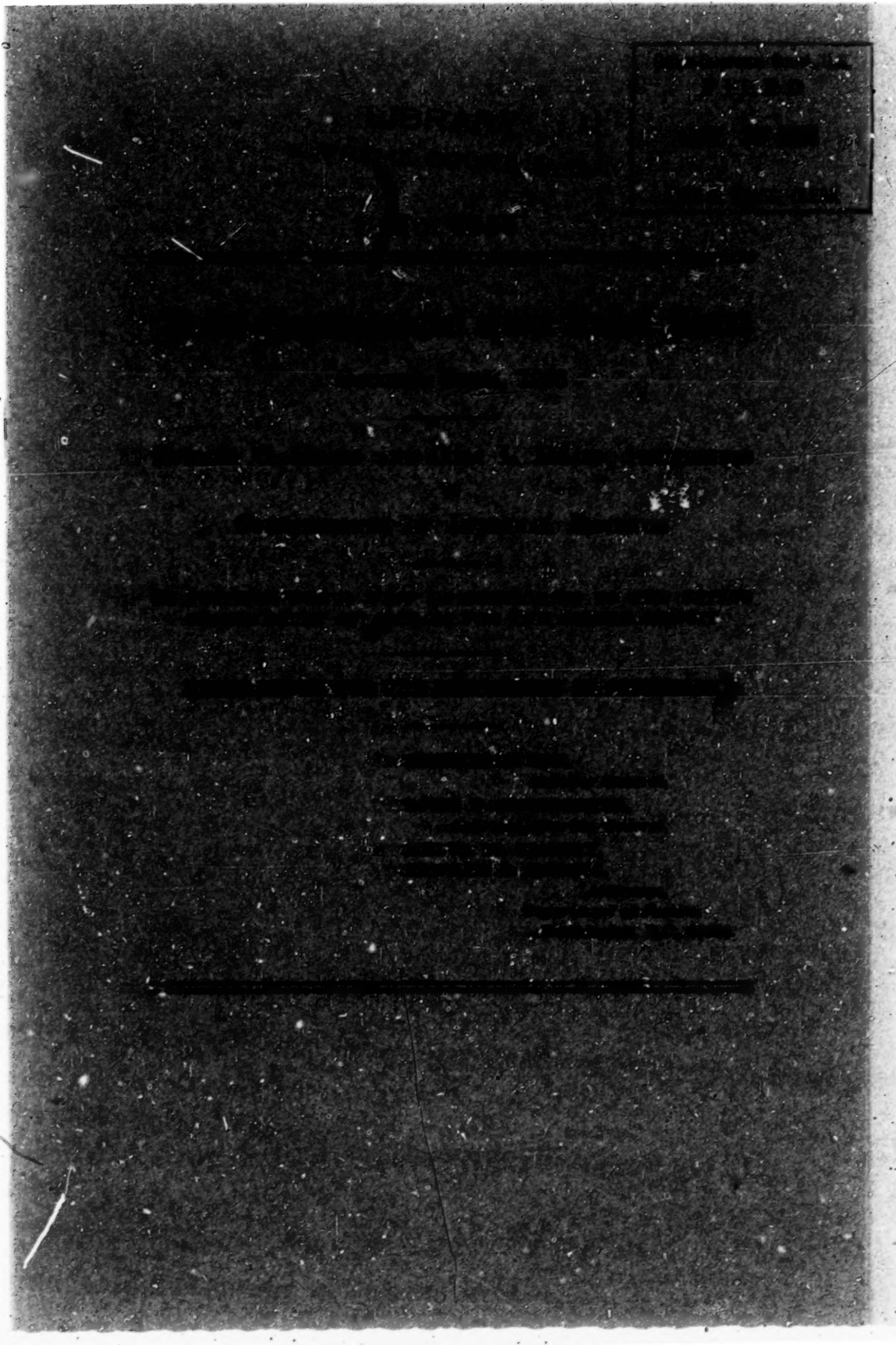
Sec. 18 [as amended by Sec. 401, Civil Service Retirement Act Amendments of 1956, c. 804, 70 Stat. 736, 743]. This Act may be cited as the "Civil Service Retirement Act."

(5 U. S. C., 1958 ed., Sec. 2251, note.)

Civil Service Retirement Act Amendments of 1956, c. 804, 70 Stat. 736, 743:

Continuation of Prior Rights.

Sec. 403. Except as otherwise provided, the amendments made by this title shall not apply in the case of employees or Members retired or otherwise separated prior to its effective date, and the rights of such persons and their survivors shall continue in the same manner and to the same extent as if this title had not been enacted. * * *.



In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 1055

EDWARD C. HEARD AND CORA L. HEARD, PETITIONERS

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE EIGHTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

For about 23 years prior to his retirement in 1952, the taxpayer, Edward C. Heard, was an employee in the Government's classified civil service. Upon his retirement, he was entitled to the benefits of the Civil Service Retirement Act, c. 349, 46 Stat. 468, as amended (5 U.S.C. (1952 ed.) 691, *et seq.*; now 5 U.S.C. 2251–2268).[1] Under the Act, he elected to receive an annuity to be paid monthly beginning May 1, 1956. By the end of 1958, the monthly payments he had received exceeded by $2,224.99 the contributions he had made to the Act's retirement

[1] For a detailed explanation of the civil service retirement system in effect as of January 1, 1954, see S. Doc. No. 89, 83d Cong., 2d Sess. (Part 1), pp. 86–103.

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fund through withholdings from his salary during his civilian service.

The Commissioner determined that $2,224.99 of the total monthly payments received by the taxpayer in 1958 was includable in the taxpayer's income under Section 72 of the Internal Revenue Code of 1954 since he had received more than the amount of his contribution within three years of first receiving benefits. The Tax Court sustained his determination. In affirming that decision, the court of appeals held that the amount in question was income within the meaning of Section 61(a) of the Code and, therefore, did not decide whether it was also taxable under Section 72. The questions presented here are (1) whether the amount of $2,224.99 referred to above is income within the meaning of the Internal Revenue Code and the Sixteenth Amendment to the Constitution; and (2) whether the inclusion of that amount in income is an unlawful discrimination against the recipients of civil service retirement benefits in light of the tax exemption granted old age and survivors insurance payments made pursuant to the Social Security Act (42 U.S.C. 301, *et seq.*).

1. The decision below that the $2,224.99 received by the taxpayer in 1958 under the Civil Service Retirement Act constitutes gross income within the meaning of Section 61(a) is correct.[2] This amount

[2] We also submit that $2,224.99 is taxable under Section 72—an issue which the court below did not find it necessary to reach (Pet. 19). This Section on its face covers all annuities and has been consistently ruled by the Commissioner to cover civil service annuity payments. See, *e.g.*, T.D. 3112, 1921-4 Cum. Bull. 76; Treasury Regulations on Income Tax (1954 Code), Sec. 1.61-11 (26 C.F.R. 1.61-11).

of the annuity payments was in excess of the taxpayer's contributions to the Act's retirement fund and thus constituted gain to the taxpayer and not a return of capital. Cf. *Manne* v. *Commissioner*, 155 F. 2d 304 (C.A. 8). Unless specifically exempted, such a gain must be taxed. *Commissioner* v. *Glenshaw Glass Co.*, 348 U.S. 426, 429–430; *United Grocers, Ltd.* v. *United States*, 308 F. 2d 634, 63[illegible] (C.A. 9); *Simpson* v. *United States*, 261 F. 2d 497, 500 (C.A. 7), certiorari denied, 359 U.S. 944; see also *Gen. Investors Co.* v. *Commissioner*, 348 U.S. 434. While the taxpayer suggests that the payments were not for services and therefore constituted a gift (Pet. 7–8), Congress, in establishing the civil service retirement system, was not acting out of disinterested generosity but, instead, was concerned with obtaining for the government the benefits of a more efficient civil service. *United States* v. *Price*, 288 F. 2d 448, 450–451 (C.A. 4); see *Commissioner* v. *Duberstein*, 363 U.S. 278, 285; *Commissioner* v. *LoBue*, 351 U.S. 243, 246. Moreover, as the court of appeals held (Pet. App. 15):

> * * * The Act specifically denominates the benefits as "an annuity;" participation in the retirement program is compulsory for most civilian Government employees; the retirement fund—from which the annuities are paid—consists basically of automatic deductions from the salaries of all participating employees and of regular appropriations by the Government; the point of time when an employee becomes entitled to his annuity depends upon his age, or date of disability, and upon his length of

> service; and the amount to which the employee is entitled is primarily based upon his salary and duration of service.

Since the payments constituted income, the Sixteenth Amendment in terms allows the tax. See *Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1, 17–19; see also *Stanton v. Baltic Mining Co.*, 240 U.S. 103, 112–113.

2. The taxpayer contends that Congress unconstitutionally discriminated against recipients of civil service retirement benefits in comparison with those who receive social security retirement payments. The short answer is that Congress provided in Section 37 of the 1954 Code for a credit against the tax otherwise owed of an amount equal to the retirement income received, multiplied by the lowest tax rate (and subject to certain other limitations and requirements set forth in Section 37). Thus, Congress has acted to end any unjustifiable discrimination which may have existed between the recipients of civil service annuity payments (who receive the credit) and of social security payments (who, since they pay no tax, receive no credit). See H. Rep. No. 1337, 83d Cong., 2d Sess., pp. 7–8, A16–A17 (3 U.S.C. Cong. & Adm. News (1954) 4017, 4032, 4152–4153); S. Rep. No. 1622, 83d Cong., 2d Sess., pp. 8–9, 165–166 (3 U.S.C. Cong. & Adm. News (1954) 4621, 4637, 4799–4801). Furthermore, Congress, in establishing the social security system was concerned with helping persons in economic need and therefore provided benefits substantially disproportionate to the length

of service rendered. On the other hand, the civil service retirement system provides benefits directly related to length of service and to the salary earned. See Hearings Before a Subcommittee of the Senate Committee on Post Office and Civil Service on S. 2875, 84th Cong., 2d Sess., p. 24. In the light of these differences in the two systems, Congress has not acted beyond its broad powers by exempting social security payments from tax while providing a tax credit for civil service retirement annuities. See *Barclay & Co.* v. *Edwards*, 267 U.S. 442, 450; *Foley Securities Corp.* v. *Commissioner*, 106 F. 2d 731, 735–736 (C.A. 8).

For the foregoing reasons, we respectfully submit that the petition for a writ of certiorari should be denied.

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